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No. 85-47 (2)

In the Supreme Court of the United States

OCTOBER TERM, 1985

LOYD WHITT, EXECUTOR OF THE ESTATE OF ELBERT B. WHITT, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether certain state law evidentiary presumptions regarding the conveyance of real property by fee simple deed were sufficient to satisfy petitioner's burden of proof in a proceeding before the Tax Court to review a deficiency determination made by the Commissioner of Internal Revenue.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. A62-A85) is reported at 751 F.2d 1548. The opinion of the Tax Court (Pet. App. A1-A61) is unofficially reported at 46 T.C.M. (CCH) 118.

JURISDICTION

The judgment of the court of appeals was entered on February 4, 1985. The petition for a writ of certiorari was filed on May 6, 1985. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

Petitioner is the executor of the estate of Elbert B. Whitt, who died on June 14, 1969. The decedent, a resident of Alabama, was a farmer during all his active life. In August 1952 and, again, in August 1959, the decedent and his wife signed certain deeds by which they purported to convey to

their children and a grandchild fee simple title to all of their farm lands. These deeds were subsequently recorded during 1963 and 1964, and in one instance, during 1970. While the deeds purported to dispose of all of his farm property, the decedent in fact continued to receive agricultural program payments until his death. Moreover, on his 1967 and 1968 income tax returns, the decedent reported income from, and claimed expenses relating to, the raising of cattle, swine and cotton. Pet. App. A9-A15, A64-A65.

Following a criminal tax investigation of the estate in 1975, petitioner filed an estate tax return with the IRS indicating that the decedent owned no real property at the time of his death. On audit of the estate tax return, the Commissioner determined that the decedent had retained until his death the use and possession of, or the right to receive income from, the farm lands deeded to his children and grandchild. The Commissioner accordingly included certain tracts of farm land in the decedent's gross estate as transfers with retained life interests under Section 2036 of the Code.[1] Alternatively, the Commissioner determined that, if any of the parcels had not been effectively transferred, the decedent owned them when he died so that their value would be includable in his gross estate under Section 2033 of the Code. Pet. App. A16, A62-A63.

As an alternative to the determinations in the estate tax notice of deficiency, the Commissioner, in order to protect the revenue, sent petitioner a gift tax notice of deficiency setting forth an inconsistent theory. In the gift tax notice of deficiency, the Commissioner determined that the decedent had transferred the tracts to his children and grandchild in 1963 and 1964 for less than full and adequate consideration.

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[1]Unless otherwise noted, all statutory references are to the Internal Revenue Code of 1954 (26 U.S.C.), as amended and in effect for the period at issue.

The Commissioner accordingly asserted alternative gift tax deficiencies against petitioner under Section 2501(a) of the Code. Pet. App. A16-A17, A63.

In the Tax Court, petitioner's primary contention was that the deeds purporting to convey the tracts in fee simple were conclusive evidence under Alabama law as to the effectiveness of the transfers. Thus, at trial, petitioner's case-in-chief consisted essentially of the introduction of 15 warranty deeds executed by the decedent conveying the parcels. Another deed was introduced whereby third parties conveyed one of the parcels to one of the decedent's sons. Petitioner also attempted to present the testimony of an attorney as to his legal opinion of the effectiveness of the deeds to transfer legal title under Alabama law. When the Tax Court excluded that testimony, petitioner, who had the burden of proof, then rested his case and left it to the Commissioner to call as witnesses all of the transferees who were available to testify. Pet. App. A21-A22, A63-A64.

The Tax Court upheld the Commissioner's deficiency determinations. In so ruling, the court rejected petitioner's arguments that the deeds were conclusive evidence as to the completeness of the transfers for federal tax purposes, noting that the tax effects of the transaction were determined by federal tax law "regardless of whether legal title passed to the grantees stated in the deeds under Alabama law" (Pet. App. A26). Finding that petitioner had failed to carry his burden to prove that eleven of the tracts (Tracts 2, 3, 4, 5, 8, 9, 10, 11, 14, 15 and 17) were effectively conveyed by the decedent prior to his death, the Tax Court concluded that the fair market value of those tracts was includable in the decedent's gross estate under Code Section 2033. The Tax Court further found that six other tracts (Tracts 1, 6, 7, 12, 13 and 16) were the subject of completed gifts in the years the deeds were recorded (1963 and 1964). Therefore, to the extent that full and adequate consideration was not paid on

the transfers of these latter six tracts, gift taxes were imposed against petitioner under Section 2501 of the Code. Pet. App. A23-A36.

The court of appeals unanimously affirmed (Pet. App. A62-A85). In so ruling, it upheld the Tax Court's conclusions that Tracts 5, 14 and 15 were includable in the decedent's gross estate under Code Section 2033, and that the estate was liable for gift taxes on the transfer of Tracts 1, 6, 7, 12, 13 and 16. As to the remaining eight tracts (Tracts 2, 3, 4, 8, 9, 10, 11 and 17), however, the court of appeals adopted the Commissioner's alternative position and concluded that these parcels were includable in the decedent's gross estate under Section 2036 (governing transfers with retained life estate) rather than under Section 2033. It accordingly affirmed the Tax Court's decision with respect to these eight parcels on that alternative ground (Pet. App. A77-A81).

ARGUMENT

The decision below is correct. Petitioner does not allege, nor is there, a conflict among the circuits on the question presented. There is no basis for further review.

1. The court of appeals correctly held that eight of the parcels were includable in the decedent's gross estate under Section 2036 of the Code. The federal estate tax attaches to property which a decedent owns outright at the time of his death (I.R.C. § 2033). It also attaches to property which a decedent has transferred for less than adequate consideration during his lifetime, if he has retained for life the possession or enjoyment of the property, or the right to income from it (I.R.C. § 2036).

Section 2036 reflects a "legislative policy of subjecting to tax all property which has been the subject of an incomplete *inter vivos* transfer." *United States* v. *O'Malley*, 383 U.S. 627, 631 (1966). Hence, the Code includes in a decedent's

gross estate all transfers which in substance are testamentary, *i.e.*, "transfers which leave the transferor a significant interest in or control over the property transferred during his lifetime." *United States* v. *Estate of Grace*, 395 U.S. 316, 320 (1969). So long as the decedent has retained during his lifetime substantial present economic benefits flowing from the property, it is includable in his estate under Section 2036. *Commissioner* v. *Estate of Holmes*, 326 U.S. 480, 486 (1946).

Here, the testimony conclusively demonstrated that the decedent placed Tracts 9, 10 and 11 in his granddaughter's name with the understanding that he would continue to farm the land and raise hogs and that he would derive the income from those properties until his death. Neither the grantee nor her guardian took possession of the land or received any income therefrom until after the decedent had died (Pet. App. A28, A69, A70). In light of this uncontroverted evidence, the court of appeals was clearly correct in concluding that these three parcels were includable in the decedent's gross estate under Section 2036 (Pet. App. A81).

As to the remaining five tracts that the court of appeals held includable under Section 2036 (Tracts 2, 3, 4, 8 and 17), petitioner had the burden of overcoming the presumption of correctness attaching to the Commissioner's determination that the decedent had retained the use of the land and the right to the income therefrom, despite the transfer of legal title. See *Helvering* v. *Taylor*, 293 U.S. 507, 515 (1935); Tax Court Rule 142(a). Petitioner, however, declined to introduce any evidence to show that the decedent had made complete deliveries of the tracts and relinquished all rights to income. To the contrary, the record affirmatively shows that the decedent was still farming at least some of the tracts (Pet. App. A9-A13). In light of this state of the record, the court of appeals correctly sustained the

Commissioner's determination that those five tracts were includable in the decedent's gross estate under Section 2036.[2]

2. Relying on certain state law presumptions regarding the conveyance of real property by fee simple deed, petitioner urges (Pet. 8-10) that he met his burden of proof in the Tax Court merely by introducing the deeds into evidence. This argument is without merit. A taxpayer cannot defeat the application of Section 2036 simply by transferring bare legal title to the objects of his affection. As the court of appeals correctly noted (Pet. App. A81), Section 2036 "presumes that legal title has been transferred," since it applies where a decedent retains enjoyment of property even though he has "made a transfer * * * [of it] by trust or otherwise" (I.R.C. § 2036(a)). And as the court of appeals also observed correctly, a transfer of bare legal title was "all that the deeds proved" here (Pet. App. A81). The burden was on petitioner to prove, as he refused to do, the nonexistence of any implied agreement that the decedent

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[2]The court of appeals also correctly affirmed the Tax Court's decision that three of the parcels (Tracts 5, 14 and 15) were includable in the decedent's gross estate pursuant to Section 2033 (Pet. App. A74-A76). That Section provides that the value of the gross estate "shall include the value of all property to the extent of the interest therein of the decedent at the time of his death." Petitioner does not challenge the court of appeals' rulings with respect to Tracts 5 and 15 (Pet. 7 n.3). With respect to Tract 14, the record shows that petitioner introduced a deed by which two individuals conveyed the property to one of the decedent's sons in 1932 (Pet. App. A35-A36). Although petitioner had ample opportunity to elicit testimony from that son about this tract at trial, he chose not to do so, thereby permitting the Tax Court to infer that the testimony would have been unfavorable to petitioner. In light of this state of the proof, the Tax Court and court of appeals were clearly correct in upholding the Commissioner's alternative determination that Tract 14 was includable in the decedent's gross estate under Section 2033 (Pet. App. A35-A36, A76). In any event, this determination is factual and warrants no further review.

retained the use of the land and the right to the income therefrom. The introduction of the deeds alone could not satisfy that burden. See *Estate of McNichol* v. *Commissioner,* 265 F.2d 667, 669-671 (3d Cir.), cert. denied, 361 U.S. 829 (1959) (fee simple deeds and state statute of frauds are not dispositive for purposes of Section 2036); *Estate of Graham* v. *United States,* 52 A.F.T.R. 2d (P-H), ¶ 148,605 (4th Cir. 1983) (deed transferring legal title to timberlands cannot defeat the application of Section 2036); *Guynn* v. *United States,* 437 F.2d 1148, 1150 (4th Cir. 1971) (to the same effect, where a house was purchased by the decedent but titled in her daughter's name).

Nor is there any substance to petitioner's further contention (Pet. 8) that the decision below conflicts with *Erie R.R.* v. *Tompkins,* 304 U.S. 64 (1938). That case held that the statutes and legal presumptions of the several states must be applied in the determination of issues of state law. See also Fed. R. Evid. 302. But *Erie* was a diversity case which involved an issue of state tort law. The controlling question here, by contrast, involves federal tax law. The courts below properly looked to federal rather than state law to determine whether the land was includable in the estate, regardless of whether some sort of legal title passed to the grantees under local law. As this Court observed in *Morgan* v. *Commissioner,* 309 U.S. 78, 80-81 (1940) (footnote omitted):

> State law creates legal interests and rights. The federal revenue acts designate what interests or rights, so created, shall be taxed. Our duty is to ascertain the meaning of the words used to specify the thing taxed. If it is found in a given case that an interest or right created by local law was the object intended to be taxed, federal law must prevail no matter what name is given to the interest or right by state law.

See also *Commissioner* v. *Estate of Holmes,* 326 U.S. at 486; *Lyeth* v. *Hoey,* 305 U.S. 188, 193, 194 (1938).

Federal tax law turns on what in fact actually happened, as proved by the taxpayer, and not on what might be presumed to have happened, in the absence of proof, in a state court. Tax Court Rule 142(a). Thus, contrary to petitioner's contentions, the procedural presumptions that might prevail in state court in certain circumstances have no bearing on petitioner's burden here to show that the decedent did not in fact retain dominion and control over the various tracts of land. To allow petitioner to satisfy his burden of proof merely by showing that he would be excused from such proof in certain types of state proceedings would be to vitiate the controlling federal requirements.[3]

3. Finally, the court of appeals correctly affirmed as not clearly erroneous the Tax Court's finding that six of the parcels (Tracts 1, 6, 7, 12, 13 and 16) constituted completed inter vivos gifts to the decedent's children in 1963 and 1964, when the deeds were recorded (Pet. App. A81-A85). For the years at issue, Section 2501(a) of the Code imposed a tax for each calendar year on the transfer of property by gift. The Treasury Regulations state that a gift is complete when "the donor has so parted with dominion and control as to leave in him no power to change its disposition, whether for his own benefit or for the benefit of another." Treas. Reg.

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[3]Petitioner also complains (Pet. 10-11) that the burden placed on him by the court of appeals required him to prove a negative—*i.e.*, that no implied agreement existed allowing the decedent to retain the use of the land or the right to its income. That consideration, however, did not warrant a decision in petitioner's favor. It is undisputed that petitioner had the burden of overcoming the presumption of correctness attaching to the Commissioner's deficiency determinations. T.C. R. 142(a). Since petitioner refused to submit any evidence other than the deeds, he can hardly complain of prejudice. If the decedent did not in fact retain the use of the land or the right to its income, that fact could have been proved by petitioner's introduction of testimony about who *did* exercise dominion and control over it.

§ 25.2511-2(b). See also *Weil* v. *Commissioner,* 31 B.T.A. 899, 906 (1934), petition denied, 82 F.2d 561, 562-563 (5th Cir.), cert. denied, 299 U.S. 552 (1936); *Gagne* v. *Commissioner,* 16 T.C. 498, 501 (1951).

Under Alabama law, all conveyances of real property "are inoperative and void as to purchasers for a valuable consideration, mortgagees and judgment creditors without notice, unless the same have been recorded before the accrual of the right of such purchasers, mortgagees or judgment creditors" (Ala. Code § 35-4-90(a) (1975)). Thus, until such time as the deeds at issue here were recorded, the decedent had it within his power to convey the land to a subsequent purchaser, who would then have had a better title to the land than the grantees. It follows, therefore, as the courts below correctly held (Pet. App. A31-A32, A83-A84), that the decedent did not put the tracts beyond recall for federal gift tax purposes until 1963 and 1964, the years in which the deeds were recorded.

Petitioner errs in contending (Pet. 10) that the gifts were completed in 1952 and 1959 because a presumption exists under Alabama law that a deed is delivered on the date of its execution. To the contrary, Alabama follows the well-settled rule that delivery is an indispensable requisite to the validity of a deed whether it be a conveyance upon a valuable consideration or a voluntary conveyance in consideration of love and affection. *Culver* v. *Carroll,* 175 Ala. 469, 57 So. 767 (1912); *Johnson* v. *Bridges,* 333 So. 2d 813 (Ala. 1976); 23 Am. Jur. 2d *Deeds* § 121 (1983). The Alabama cases cited by petitioner (Pet. 5 n.1) dealing with presumptions regarding delivery all involve situations where deeds were either delivered to or acknowledged by the stated grantees. *Carroll* v. *Carroll,* 236 Ala. 556, 183 So. 857 (1938); *William* v. *Armstrong,* 130 Ala. 389, 30 So. 553 (1901). In any event, the contention concerns a question of state law that does not warrant this Court's review.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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